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Turning the Corner: The Economic Revival of Central Asia

Central Asia seems to have turned the corner during the last few years. Economic growth, which accelerated to historically unprecedented levels, has been driven by high commodity prices - particularly oil and natural gas - and buyout demand, increasing inward investment, improved macroeconomic management and development of infrastructure.

This paper reviews the characteristics of the boom that has evolved since 1997, with particular reference to macroeconomic developments and poverty. Distinctions are drawn between the economic structure and performance of resource rich (oil and natural gas) economies and the other CARs who have fewer resources. Drawing on this analysis, the outlook for the CARs for the next ten years is projected against a background of global prospects. The paper also seeks to guide CARs policy makers by suggesting the direction of future economic performance as well as indicating key policy issues. As long run forecasts can change in response to external events, the risks to the CARs outlook are also highlighted.

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Content

Turning the Corner: The Economic Revival of Central Asia

Malcolm Dowling and Ganeshan Wignaraja[1]

1. Introduction

The Central Asia Republics (CARs) occupy a strategic position straddling East and West and have a significant development potential. In the aftermath of transition, however, the CARs witnessed a period of prolonged slow and negative growth and a rising incidence of poverty[2]. Many factors have been put forward to explain the difficult transition experience including disruption in production and marketing relations with the former Soviet Union, collapse of aid from the former Soviet Union, a nascent private sector, the lack of capital markets, limited institutions required for a market economy and gaps in infrastructure.

The Central Asia Republics (CARs) occupy a strategic position straddling East and West and have a significant development potential

Nevertheless, Central Asia seems to have turned the corner during the last few years. Economic growth, which accelerated to historically unprecedented levels, has been driven by high commodity prices - particularly oil and natural gas - and buyout demand, increasing inward investment, improved macroeconomic management and development of infrastructure[3]. There are signs that oil and gas sector led

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[1] The authors are respectively Visiting Professor at Singapore Management University, Singapore and Senior Economist, Asian Development Bank, Manila. The views expressed in the paper are solely the responsibility of the authors and cannot be attributed to the organizations to which they belong.

[2] A plethora of literature exists on the history, strategic significance, economic record and reform experience of Central Asia during the first decade of transition to a market economy. For a selection see: Starr (1996 and 2004), Trushin and Trushin (2000), Pomfret and Anderson (2001), Campos and Coricelli (2002), World Bank (2002), Zhukov (2002), and Loukoianova and Unigovskaya (2004).

[3] In its first regional economic outlook for the Middle East and Central Asia, the IMF notes that "A favorable external environment combined with generally sound economic policies to produce strong macroeconomic performance for the countries of the Middle East and Central Asia in 2003 and early 2004…Prospects are for continued strong performance through 2005" (IMF, 2004, p. 2).

growth has stimulated the development of services sector (construction and banking) as well as some manufacturing activities. There are also indications that economic prosperity has been accompanied by job creation and some reduction in poverty. There is optimism in policy circles in Central Asia with some even predicting that the region will join the ranks of middle income countries within a decade or so.

Against this backdrop, this paper reviews the characteristics of the boom that has evolved since 1997, with particular reference to macroeconomic developments and poverty. Distinctions are drawn between the economic structure and performance of resource rich (oil and natural gas) economies and the other CARs who have fewer resources. Drawing on this analysis, the outlook for the CARs for the next ten years is projected against a background of global prospects. The paper also seeks to guide CARs policy makers by suggesting the direction of future economic performance as well as indicating key policy issues. As long run forecasts can change in response to external events, the risks to the CARs outlook are also highlighted.

2. Accelerating Economic Performance

Growth and Inflation. After nearly a decade of dismal economic performance following the breakup of the Soviet Union the Central Asian republics have put together a booming economic performance since 1997. From 1997 to 2001 GDP grew by nearly 6 percent per annum compared with negative growth in the previous five years (see Table 1). In the next three years growth accelerated to a spectacular 9.7 per cent, the highest in the post-transition period for any group of countries in the Soviet sphere and a performance that compares favorably with the fastest growing economies in Asia and the rest of the developing world.

High energy prices and investments in the oil and gas sector, including petrochemicals were the main growth drivers in the three oil exporting economies

High energy prices and investments in the oil and gas sector, including petrochemicals were the main growth drivers in the three oil exporting economies of Azerbaijan, Kazakhstan and Turkmenistan. In Azerbaijan oilfield and pipeline investment as well as natural gas development have contributed to a strong growth environment. In Kazakhstan oil and natural gas investments have been a source of rapid expansion. In addition economic diversification has begun recently as food processing, machinery, oil refining and chemicals showed strong growth. In Tajikistan the end of civil war served as the main impetus for expansion as GDP growth averaged about 10 percent during 2002-2004.

Among the non-oil economies growth in Kyrgyz Republic averaged around 5 percent beginning in 1997 and accelerated further to 7 percent in 2003 and 2004. A buoyant minerals sector led by gold exports expanded rapidly. Uzbekistan's economy grew steadily at just over 5 percent beginning in 1997 as agricultural production benefited from restructuring and privatization, as well as from favorable cotton prices. Per capita income has also grown dramatically as population growth has been low. By the end of 2003 per capita income increased to an average of $840.8[4].

Macroeconomic stability, proxied by inflation has also improved

Macroeconomic stability, proxied by inflation has also improved**.** Inflation rates have fallen significantly throughout the region over the past few years indicating improved macroeconomic stability. Average inflation for the CARs as a group declined from 20.4 per cent to 6.9 per cent between 1997-2001 and 2002-2004. Furthermore, both oil exporters and non oil exporters were typically able contain inflation at lower levels in 2002-2004 than in 1997-2001. This may be partly the result of greater fiscal and monetary discipline as well as greater stability in the exchange rate and moderate inflation worldwide. Kyrgyz Republic (3 per cent) had the lowest inflation among the CARs in 2002-2004 while Tajikistan, with double-digit inflation, had the highest. Inflation in Mongolia and Armenia also fell to low levels between the two sub-periods.

The share of industry in GDP and manufacturing value added increased

Structural Change. This boom has been driven by structural changes in the economies and has resulted in a shift toward production of industrial goods and minerals and away from agriculture[5]. While oil and gas continue to drive the industrial

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4 Despite these recent gains in income growth, per capita income in the CARs remains low by international standards as they are categorized as low income countries (with the exception on Kazakhstan, which is a middle income country).

5 Nevertheless, the pace of structural change in Central Asia has been slower than those witnessed in the high performing Asian economies such as South Korea, Malaysia and the Peoples Republic of China. See Wignaraja and Taylor (2003).

sector, the rest of the industrial sector and manufacturing also grew rapidly. The share of industry in GDP and manufacturing value added increased. For example manufacturing value added increased by over 25% per annum in Azerbaijan and 10% per annum in Kazakhstan between 1998 and 2003. Manufacturing value added per capita also increased. By 2003 Kazakhstan had the largest industrial base while Kyrgyz Republic had the smallest. The remaining CARs fall in between these extremes.

By 2003, manufactured exports per capita in Kazakhstan were more than three times higher than those of the other CARs

The recent industrial recovery in the CARs is closely linked to the performance of manufactured exports that grew about 10% per annum for the region as a while between 1998 and 2003. Both oil and non-oil exporters had respectable manufactured export growth although the former (11.0%) was somewhat higher than the latter (7.8%). By 2003, manufactured exports per capita in Kazakhstan were more than three times higher than those of the other CARs (see Table 1). The structure of manufacturing and manufactured exports varies from country to country. Textiles and garments comprise over 80 per cent of manufactured exports in Tajikistan and Turkmenistan (driven in part by foreign investors from Turkey and Korea) and about 37 per cent of Kyrgyz Republic's manufactured exports. Meanwhile, Kazakhstan's manufactured exports are dominated by iron and steel with some focus on chemicals and plastics as well as machinery and transport equipment. Azerbaijan also has a mix of iron and steel, chemicals and machinery.

Between 1997 and 2004 overall export growth from the oil exporting CARs was strong, averaging about 18 percent per annum

External Developments. External sector performance has generally improved compared with the past as exports have grown more rapidly. This improved trade performance, particularly since 1997 has been driven by developments in the minerals and metals sector in oil exporting countries and by prices for gold and cotton in the non-oil exporting economies. Manufacturing has also been buoyant and the overall performance has improved dramatically from a decade ago. Between 1997 and 2004 overall export growth from the oil exporting CARs was strong, averaging about 18 percent per annum. For the non-oil exporting countries in the region export performance accelerated after 2001. By 2004 export growth in Kyrgyz Republic, Tajikistan and Uzbekistan averaged over 20 percent. In Kyrgyz Republic, export growth has fluctuated from negative to strong growth, primarily because of movements in gold prices and exports of gold and petroleum products. In

Tajikistan, exports of cotton and aluminum steadily increased as the economy continues to recover. In Uzbekistan export growth picked up strongly in 2003 and 2004 on the back of higher prices for gold and cotton.

The boom has increased government revenue and has helped fiscal performance and reduced reliance on external borrowing

The boom has increased government revenue and has helped fiscal performance and reduced reliance on external borrowing. As a result the total debt for the CARs has typically fallen as a percent of GDP. In 2004 the total debt of the region (aside from Kazakhstan) was just over $8 billion and it has not increased substantially since the late 1990s. The debt service ratio was highest in Tajikistan and Kazakhstan at 49 percent and 26 percent respectively in 2004 and less than 20 percent in the other countries. A worrisome development in Uzbekistan is that the debt service ratio has been increasing steadily.

Most of Central Asia's FDI since the mid-1990s has gone to Kazakhstan, which has by far the largest potential for further economic development

There are also signs that foreign investors are beginning to take greater interest in the CARs. This is reflected by strong inflows into the oil rich exporters. This is a classic example of natural resource seeking FDI (mainly from the United States, EU and Russia) and has brought with it capital, foreign technology and western management expertise to facilitate the efficient development of oil and gas exports. Most of Central Asia's FDI since the mid-1990s has gone to Kazakhstan, which has by far the largest potential for further economic development. Such FDI is concentrated in the oil and gas industry but has gradually spilt over into electricity, metals, manufacturing and banking. In the last two years, however, there has also been a dramatic increase in FDI flows to Azerbaijan to the extent that by 2003 FDI of $2.3 billion slightly exceeded that in Kazakhstan ($2.2 billion).

It is striking that FDI in the three non-oil exporting CARs is negligible; amounting to only $107.5 million in 2003. A lack of natural resources, high transactions costs due to landlocked terrains, vast distance from markets and perceived political risk are among the explanations for limited FDI in non-oil exporting CARs.

Despite these recent gains in income growth, per capita income remains low by international standards

Per Capita Income and Poverty. Despite these recent gains in income growth, per capita income remains low by international standards. In current dollar terms, four out of the six CARs had per capita income of $600 or less per year in 1997-2001 and these levels were less than those achieved by China at the time. As Table 1 shows, by 2003 Kazakhstan and Turkmenistan were able to raise per capita income to over $1200 per capita and the other CARs were also able to make some progress. However, exchange rate movements negated some of these gains.

Growth in government revenue has enabled governments in the CARs to increase spending on programs in the human resources area. As a result there has been a gradual improvement in social sector spending for health and education. These expenditures, along with more rapid economic growth, have resulted in an improvement in human resource development indicators and a reduction in poverty.

Growth in government revenue has enabled governments in the CARs to increase spending on programs in the human resources area

Poverty line estimates are useful for cross country comparisons and reveal a variable pattern of poverty incidence in the CARs. Based on estimates made in the late 1990s and early years of the new millennium, national poverty line estimates show that between 25% and 30% of the population was in poverty in two oil exporting CARs – Kazakhstan and Turkmenistan - and in Uzbekistan (see Table 1). In the remaining three CARs (Azerbaijan, Kyrgyz Republic and Tajikistan) poverty estimates were nearly twice as high, ranging from around 50% to 56%. For the CARs as a whole, poverty averages around 41%. Poverty has fallen somewhat in Kazakhstan, where estimates of poverty made in the late 1990s were in the range of 40%. It is difficult to determine trends in poverty in the other CARs based on national estimates due to lack of data. It is worthwhile noting that international poverty line estimates made by the World Bank show somewhat lower levels of poverty and that poverty has been declining slowly[6].

For the CARs as a whole, poverty averages around 41%

3. Future Outlook

The pressing question facing the CARs is whether the boom that started in the late 1990s will continue for the next decade.

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[6] Although the data is very sketchy and there are issues of data consistency and reliability, the available international poverty line estimates suggest that poverty has declined in several CARs. It seems that greater economic prosperity in recent years has spilt over into employment creation and some reduction in poverty in the region. Furthermore, it seems that the oil exporters typically have a lower poverty incidence than the non-oil exporters. For details see ADB (2005).

While this is impossible to predict with certainty, we offer a possible outcome, which we believe is most likely.

World Outlook. The projections for the CARs are made based on certain assumptions about the future direction of the world economy. The World Outlook is developed with the aid of a world econometric model developed by Oxford Economic Forecasting (OEF 2005). These can be summarized as follows:

- Robust world growth of about 3.3 percent and buoyant global demand.
- Favorable commodity prices including oil prices of about \$35 per barrel.
- The emergence of China and India as regional economic powerhouses.
- No wars or big disruptions in the region.
- Growing investor confidence (particularly with regard to foreign direct investment).
- A continuation of the agenda for policy reform at a moderate pace and that the CARs will continue to make reforms.

GDP growth in the region is likely to be robust, averaging 7.2% per annum in all the CARs (2005-2015)

These forecasts form the global macroeconomic background for the analysis of future prospects for the CARs. We derived our forecasts for the CARs based on initial conditions (e.g. resource endowments and human capital) and the expected pace of implementation of policy reforms. Where events seemed to be smoothly evolving, time trends were used for projections. In other cases, structural changes were incorporated to provide a more comprehensive framework[7].

Growth. As Table 2 shows, GDP growth in the region is likely to be robust, averaging 7.2% per annum in all the CARs (2005-2015). This is quite high by the historical standards of developing and transition countries. As a group, the oil rich economies will grow more rapidly than the non-oil economies. Azerbaijan is expected to grow the fastest at around 11% per annum and Uzbekistan the slowest (5% per annum). In between these, Kazakhstan is likely to grow at 7.4%, Tajikistan 6.1%, Kyrgyz

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[7] For more details see ADB (2005).

Republic 5.8% and Turkmenistan 5.8%. This is a strong performance for developing countries in general and even by comparison with Asian transition economies such as Viet Nam, Cambodia and Laos. Robust growth combined with different endowments and development opportunities suggest that the CARs will emerge as one of world's most dynamic developing regions. There will be significant potential for structural changes and a number of opportunities for trade and international investment in manufacturing and also in the booming oil and gas industry.

Structural Change. Structural changes will occur as a result of increased exploitation of the mineral resource base and the process of industrialization that is projected to continue. By 2015, total oil and gas exports from the oil rich CARs will amount to about $32 billion, a nearly three fold increase from export value of about $12 billion today[8]. Oil and gas exports will continue to be the main drivers of economic growth and dynamism in the three oil rich economies. Proven reserves of oil and natural gas should be sufficient to maintain current and projected future rates of extraction for between 25 and 60 years in the three oil exporting economies. Growth in oil and gas exports will be strongest in Azerbaijan following the opening of the Baku-Tbilise-Ceyhan (BTC) pipeline to Turkey. This pipeline opens up the European oil market to Azerbaijan and potentially also to Kazakhstan. The BTC pipeline will provide an alternative oil shipment route to Europe avoiding the high transit charges levied by the Russian Federation. Oil sector growth will slow somewhat in the medium term as prices for oil and gas stabilize at around $35 per barrel and output growth slows as existing pipeline capacity is more fully utilized. Nevertheless, the oil and gas sector will grow faster than the GDP in all oil exporting countries.

By 2015, total oil and gas exports from the oil rich CARs will amount to about $32 billion

Economic diversification will continue at a more rapid pace through the expansion of manufactured exports. As Tables 1 and 2 suggest total manufactured exports per head in the CARs is projected to nearly treble to $141 by 2015 (up from $57.1 in 2003). The region's manufactured export base will continue to

Total manufactured exports per head in the CARs is projected to nearly treble to $141 by 2015

[8] These projections were based on forecasts of oil prices, production capacity, proven reserves and anticipated developments in transportation (e.g. pipelines).

be dominated by Kazakhstan ($ 4.8billion) and Uzbekistan ($2.5 billion). Kazakhstan will continue to have the highest manufactured exports per head. Turkmenistan comes next. Azerbaijan remains the smallest exporter in terms of manufactured exports per head. Capital-intensive petroleum products like plastics and petrochemicals, metal products, engineering goods and some textiles and garments are likely to underlie this manufactured export growth. There is also likely to be diversification of export markets away from Russia as demand from China and India grow rapidly. Industrialization and structural change will result in a wider variety of products being produced for regional and international markets, help boost per capita income and result in job creation.

The current account deficit is projected to increase in Kyrgyz Republic and Tajikistan

External Sector. The external sector projections focus on the three non oil-exporting countries (Kyrgyz Republic, Tajikistan and Uzbekistan). This is because the external sector accounts for the three oil-producing countries are dominated by oil and gas. As a result these countries have high enough incomes and sufficient foreign direct investment to go to capital markets for additional resources. The current account deficit is projected to increase in Kyrgyz Republic and Tajikistan. These current account deficits will be modest in size, ranging from $200 million per annum in Kyrgyz Republic to $70 million in Tajikistan for the period 2011 - 2015. This is because import demand growth to meet various infrastructure and manufacturing project requirements as well as for some consumer goods is projected to be somewhat stronger than the expansion of exports proceeds. Growth in the current account deficit will be constrained by already high levels of external debt and limited sources of finance for Kyrgyz Republic and Tajikistan. In Uzbekistan the current account balance is projected to remain in surplus over the forecast period as a result of stronger export growth to the Chinese market and continued slow growth in imports. Structural factors and a restrictive policy environment that discourages trade liberalization will also inhibit more rapid import growth.

The slower reforming policy environment in Uzbekistan is expected to keep inflows of FDI growth to around $120 million per annum

Foreign direct investment (FDI) is expected to rise slowly as the external policy environment improves in Kyrgyz Republic and (to a lesser extent) in Tajikistan. FDI inflows of $125 million per annum in Kyrgyz Republic and $75 million in Tajikistan, while modest in size by international standards, will help to offset the rising current account deficit and should contribute to growth technology transfer and productivity gains in industry. The slower reforming policy environment in Uzbekistan is expected to keep inflows of FDI growth to around $120 million per annum.

Total outstanding debt as a percent of GDP is expected to decline slowly in Kyrgyz Republic and Tajikistan and more rapidly in Uzbekistan. The drivers for debt reduction are increased inflows of FDI in all three non-oil economies, debt restructuring in Kyrgyz Republic and possibly Tajikistan, remittances in Tajikistan and the use of some trade and current account surplus to reduce external debt in Uzbekistan.

Per Capita Income and Poverty. Average per capita income for the CARs of just under $2,000 in 2015 will place the region firmly within the ranks of today's middle-income economies[9]. However, there will be significant variation within the region with the oil rich economies, led by Kazakhstan, having per capita incomes more than six times higher than those of the non-oil economies (see Table 2). With a per capita income of $5,248 by 2015, Kazakhstan will be firmly established as an upper middle-income country. The other two oil rich economies per capita income will be comparable to the current per capita income of Russia and Thailand. Tajikistan (per capita income of $375) will remain the poorest CAR and be among the ranks of the today's low income countries ($450 per head). With just under $600 per head, Kyrgyz Republic and Uzbekistan will be somewhat higher and have graduated into the category of lower middle-income countries. Nevertheless they will remain among the low-income countries in terms of per capita income levels. These forecasts highlight the impact of successful exploitation of oil and gas resources and indicate that there will be increased divergence in the economic prosperity between oil and non-oil rich economies. They also underline the likely emergence of Kazakhstan as a regional growth pole with the potential to drive expanded trade and investment relationships with other CARs. Kazakhstan and the two oil rich economies will also increasingly become a magnet for labor migration from poorer CARs. For the non oil economies of Tajikistan, Uzbekistan and Kyrgyz Republic there will be a

Kazakhstan and the two oil rich economies will also increasingly become a magnet for labor migration from poorer CARs

[9] Zhukov (2000), p. 254, says that to restore income to 1990 levels, the CARs will have to grow at between 4.5 and 5 per cent per annum until 2015.

Rapid growth in income will facilitate a sustained reduction in poverty in the CARs over the forecast period

continued need for external assistance to raise incomes and reduce the impact of poverty.

Rapid growth in income will facilitate a sustained reduction in poverty in the CARs over the forecast period. As a whole the incidence of poverty will fall from 40.6% today to about 23.8% in 2015 (see Tables 1 and 2)[10]. This means that there will be around 12 million more people will be taken out of poverty as a result of strong economic performance. While still high, this rate of poverty is around the current level of poverty in Poland today and slightly less than the current rate of poverty the Russian Federation. The poorest country in 2015 will remain Tajikistan, which will have about a third of its population below the poverty threshold. The Kyrgyz Republic will have a somewhat lower incidence of poverty followed by several other CARs that will be able to bring poverty down to the range of 15%-18%. In all the CARs rural poverty will remain higher than urban poverty while pockets of urban poverty are likely to persist. The analysis of future trends in poverty suggests that high rates of rural poverty will continue to stimulate rural to urban migration and that international migration is likely to continue at a significant rate. Even though poverty reductions will be substantial some of the poorer CARs will need to devote more resources to reducing poverty by expanding current programs to fight poverty and developing new programs to address the needs of specific target groups. The development of labor-intensive sectors such as agriculture and tourism would also contribute to poverty reduction.

The analysis of future trends in poverty suggests that high rates of rural poverty will continue to stimulate rural to urban migration…

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[10] A crucial aspect of the poverty projection for 2015 was the elasticity of poverty reduction with respect to GDP growth. The reported poverty estimates are somewhat conservative considering the development experience of other Asian economies. Oil exporting countries were assumed to have somewhat lower poverty elasticities due to the capital intensity of oil sector and industrial production. Remittance income from overseas workers in the non-oil economies are also taken into account in making poverty assessments for the future. These projections were based on historical information for the CARs, staff estimates of structural change in the poverty-income relationship over time and poverty elasticity's for other Asian countries. On other Asian Countries and other developing countries in general see Dowling and Valenzuela (2004).

4. Risks

There are two fundamental sources of risks to the forecasts contained in this paper. The first relates to prospects for the world economy, particularly industrial countries. The second involves the CARS themselves.

Much of the income added to the world economy in the past few years was from China' rapid growth

Risks to the global economy. There are a number of risks to the forecast that could result in lower growth and poor economic performance of the world economy. Persistent higher oil prices are the most immediate threat. Higher oil prices will slow down growth in the United States and other industrial countries, which will have an adverse effect to the rest of the world through international trade. Another risk relates to future economic performance in China. Much of the income added to the world economy in the past few years was from China' rapid growth, a trend which is built into our forecast. If China is not able to slow its growth gradually it could result in a sharp economic slowdown that could have serious repercussions on world growth and the rest of Asia.

Risks to the CARs. There are several risks to the outlook for the CARs. Some of these risks relate to the outlook for the world economy. These include sluggish growth or a collapse in energy prices and/or weakness in the major commodity exports of the CARs including cotton, aluminum and gold. Terrorism is a continuing potential threat to the region, particularly where ethnic tensions could surface. Political instability and poor governance pose considerable risks to the CARs outlook. Particularly relevant is the prospect of prolonged economic and political uncertainty in the Kyrgyz Republic following the sudden change of government, political protests in Azerbaijan and escalating tensions in Uzbekistan in the wake of the Andijan crackdown.

Political instability and poor governance pose considerable risks to the CARs outlook

At the policy level the timing of structural and policy reforms envisaged in the outlook could be delayed or postponed. These include regional cooperation arrangements in the oil and natural gas sector that would increase revenue and reduce transit taxes as well as general regional cooperation measures to deal with trade and transit bottlenecks. Reforms in the non oil economies that would lift productivity, contribute to diversification of the industrial base and increase efficiency may also be delayed. Slower economic growth or slower implementation of initiatives to address social sector issues would also have an adverse impact on anticipated reductions in poverty.

5. Summary and Policy Implications

The overall outlook for Central Asia up to 2015 is positive

The overall outlook for Central Asia up to 2015 is positive. The region seems set to join the ranks of middle-income countries driven by robust GDP growth in excess of 7% per annum in the CARs. Furthermore, poverty will fall dramatically to about 23% of the region's population. The oil and gas sector will underlie economic prosperity alongside an emerging private manufacturing sector. At the same time, some outstanding challenges will remain. In spite of rapid growth, poverty levels will be unacceptably high in several Central Asian countries. The nascent manufacturing sector and particularly private enterprises need to be supported by business friendly policies. Slow population growth means that the domestic market and skill base might have to be enhanced by regional cooperation and labor migration.

The realization of this positive outlook will depend upon a number of factors

The realization of this positive outlook will depend upon a number of factors. Some are driven by external influences while others are within the realm of policy makers. There are three principle policy priorities which require initiatives at the national level as well as regional cooperation within the CARs.

On the energy side this will require a transparent, predictable policy environment…

Continued development of the region's energy resources while further diversifying the economy. On the energy side this will require a transparent, predictable policy environment to attract continued inward investment, rationalization of power prices to reflect cost consideration, development of pipelines featuring both national and regional priorities, judicious investment of energy resources and environmental management to best international standards[11]. Key priorities for industrial diversification might include: small and medium enterprise development through financial and non-financial support, attraction of export-oriented foreign investment through competitive incentives and more aggressive promotion, streamlining of business procedures and encouraging spillovers from oil and gas industries.

[11] For an analysis of some of the policy issues in the oil and gas sector of Kazakhstan see Khusainov and Berentaev (2004).

Development of Cost-Competitive Infrastructure including Regional Cooperation. Given the distance from international markets, it is critical to improve infrastructure. Some of the projects could include: improvements in the internal and external road network; expand, harmonize and modernize the railway network; invest in ICT infrastructure; and ensure free and flexible air transport. Small and segmented domestic markets, high infrastructure development costs, transit bottlenecks and dispersed resource endowments make regional cooperation crucial to future prosperity. Some initiatives might include: reduction of barriers to regional trade and investment, harmonization of regional customs administration, resolution of disputes over the water-energy nexus and further co-operation to resolve problems in transport of energy via pipelines.

Given the distance from international markets, it is critical to improve infrastructure

Poverty Reduction. The persistence of poverty requires special attention in future economic strategy. Measures to reduce poverty further might include: providing targeted provision for groups at risk, expanding the provision of micro-finance, increased expenditure on social sectors targeting the poor, and education of women. The development of labor intensive sectors such as agriculture and tourism would also contribute to poverty reduction.

The persistence of poverty requires special attention in future economic strategy

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Table 1. Current Economic Performance in Central Asia

Country	Real GDP Growth % per year		Manufactured exports per capita, $	Per Capita Income, $	Poverty Incidence, % of population (b)
	1997-2001	**2002-2004**	**2003**	**2003**	**Latest**
Oil Exporters					
Azerbaijan	9.5	10.6	16.4	865.0	49.6
Kazakhstan	5.2	9.5	142.1	1,995.0	27.9
Turkmenistan	10.2	21.3	46.9	1,236.0	29.9
Non-Oil Exporters					
Kyrgyz Republic	5.3	4.7	38.2	344.0	52.0
Tajikistan	5.9	9.9	39.7	207.0	56.6
Uzbekistan	4.4	5.3	30.7	389.0	27.5
CARs	(a) 6.1	(a) 9.7	57.1	839.3	40.6

Notes: (a) Weighted average, GDP weights. (b) National poverty lines

Sources: Calculated from ADB Asian Development Outlook, various; ADB (2004); World Bank World Development Indicators 2005; national sources.

Table 2. Future Prospects in Central Asia

Country	**Real GDP Growth 2005-2015 % per year**	**Manufactured exportsper capita, $ 2015**	**Per Capita Income, $ 2015**	**Poverty Incidence 2015, % of population (b)**
Oil Exporters				
Azerbaijan	11.2	37.4	2,829	26.6
Kazakhstan	7.5	365.3	5,248	16.3
Turkmenistan	5.8	136.2	1,959	18.1
Non-Oil Exporters				
Kyrgyz Republic	5.8	57.4	593	32.9
Tajikistan	6.1	83.0	375	31.3
Uzbekistan	5.2	82.3	591	17.8
CARs	7.2 (a)	141	1,933	23.8

Notes: (a) Weighted average, GDP weights. (b) National poverty lines

Source: Authors estimates

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